

**§ 1.1016-4 Exhaustion, wear and tear, obsolescence, amortization, and depletion; periods during which income was not subject to tax.**

(a) Adjustments to basis must be made for exhaustion, wear and tear, obsolescence, amortization, and depletion to the extent actually sustained in respect of:

(1) Any period before March 1, 1913.

(2) Any period since February 28, 1913, during which the property was held by a person or organization not subject to income taxation under chapter 1 of the Code or prior income tax laws.

(3) Any period since February 28, 1913, and before January 1, 1958, during which the property was held by a person subject to tax under part I, subchapter L, chapter 1 of the Code, or prior income tax law, to the extent that section 1016(a)(2) does not apply, and

(4) Any period since February 28, 1913, during which such property was held by a person subject to tax under part II of subchapter L, chapter 1 of the Code, or prior income tax law, to the extent that section 1016(a)(2) does not apply.

(b) The amount of the adjustments described in paragraph (a) of this section actually sustained is that amount charged off on the books of the taxpayer where such amount is considered by the Commissioner to be reasonable. Otherwise, the amount actually sustained will be the amount that would have been allowable as a deduction:

(1) During the period described in paragraph (a) (1) or (2) of this section, had the taxpayer been subject to income tax during those periods, or

(2) During the period described in paragraph (a) (3) or (4) of this section, with respect to property held by a taxpayer described in that paragraph, to the extent that section 1016(a)(2) was inapplicable to such property during that period.

In the case of a taxpayer subject to the adjustment required by subparagraph (1) or (2) of this paragraph, depreciation shall be determined by using the straight line method.

[T.D. 6681, 28 FR 11131, Oct. 17, 1963]

**§ 1.1016-5 Miscellaneous adjustments to basis.**

(a) *Certain stock distributions.* (1) In the case of stock, the cost or other basis must be diminished by the amount of distributions previously made which, under the law applicable to the year in which the distribution was made, either were tax free or were applicable in reduction of basis (not including distributions made by a corporation which was classified as a personal service corporation under the provisions of the Revenue Act of 1918 (40 Stat. 1057) or the Revenue Act of 1921 (42 Stat. 227), out of its earnings or profits which were taxable in accordance with the provisions of section 218 of the Revenue Act of 1918 or the Revenue Act of 1921). For adjustments to basis in the case of certain corporate distributions, see section 301 and the regulations thereunder.

(2) The application of subparagraph (1) of this paragraph may be illustrated by the following example:

*Example:* A, who makes his returns upon the calendar year basis, purchased stock in 1923 for \$5,000. He received in 1924 a distribution of \$2,000 paid out of earnings and profits of the corporation accumulated before March 1, 1913. The adjusted basis for determining the gain or loss from the sale or other disposition of the stock in 1954 is \$5,000 less \$2,000, or \$3,000, and the amount of the gain or loss from the sale or other disposition of the stock is the difference between \$3,000 and the amount realized from the sale or other disposition.

(b) *Amortizable bond premium*—(1) *In general.* A holder's basis in a bond is reduced by the amount of bond premium used to offset qualified stated interest income under § 1.171-2. This reduction occurs when the holder takes the qualified stated interest into account under the holder's regular method of accounting.

(2) *Special rules for taxable bonds.* A holder's basis in a taxable bond is reduced by the amount of bond premium allowed as a deduction under § 1.171-3(c)(5)(ii) (relating to the issuer's call of a taxable bond) or under § 1.171-2(a)(4)(i)(A) (relating to excess bond premium).

(3) *Special rule for tax-exempt obligations.* A holder's basis in a tax-exempt obligation is reduced by the amount of